SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1941

No. 913

AMERICAN CHICLE COMPANY,
Petitioner,

vs.

THE UNITED STATES.

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

ERWIN N. GRISWOLD,
Counsel for Petitioner.

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PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

The undersigned, on behalf of the American Chicle Company, prays that a writ of certiorari issue to review the judgment of the United States Court of Claims entered in the above cause on November 3, 1941.

Opinion Below.

The findings of fact and opinion of the Court of Claims (R. 14-24) are reported in 41 F. Supp. 537.

Jurisdiction.

The judgment of the Court of Claims was entered on November 3, 1941 (R. 25). The jurisdiction of this Court

is invoked under Section 3(b) of the Act of February 13, 1925.

Question Presented.

Under § 131(f) of the Revenue Act of 1936 and 1938, providing, for the purposes of the foreign tax credit, that a domestic corporation shall be deemed to have paid that proportion of the foreign taxes paid by a foreign subsidiary upon or with respect to its "accumulated profits" which the amount of dividends paid by the subsidiary bears to the amount of such "accumulated profits," is the foreign tax deemed to have been paid by the parent to be determined by the formula,

$$\frac{\text{Dividends}}{\text{Accumulated profits}} \times \text{total foreign tax}$$

as the petitioner contends, or by the formula,

$$\frac{\text{Dividends}}{\text{Total Profits}} \times \text{total foreign tax}$$

as the respondent contends and the Court below held?

Statute Involved.

The statute involved is § 131(f) of the Revenue Acts of 1936 and 1938, which is the same in both Acts. Neither statute is different in any respect material to this case from § 238(c) of the Revenue Act of 1921, and the corresponding provision in every subsequent Revenue Act to date.

The text of § 131(f) of the Revenue Acts of 1936 and 1938 is set forth in the appendix (*infra*, pp. 10-11).

Statement.

The action was filed below to recover income taxes for the calendar years 1936, 1937 and 1938. The facts found by

the Court of Claims (R. 14-18) may be summarized as follows:

During the years 1936 and 1937, the petitioner was the sole stockholder of two foreign subsidiaries, the Canadian Chewing Gum Company, Ltd., and the American Chicle Company of Mexico, S. A. and during the year 1938, it was the sole stockholder of the Canadian Chewing Gum Company, Ltd., the Canadian Chewing Gum Sales, Ltd., and Chicle Adams, S. A., all foreign corporations (R. 15). In computing the petitioner's foreign tax credit under § 131 of the Revenue Acts on account of taxes paid by these subsidiaries, the Commissioner of Internal Revenue used the following formula (R. 15):

$$\text{Foreign tax accrued or paid} \times \frac{\text{Accumulated profits of subsidiary}}{\text{Total profits of subsidiary}} \times \frac{\text{Dividends received}}{\text{Accumulated profits of subsidiary}} = \text{Credit allowable under § 131(f)}$$

On December 21, 1939, the petitioner filed three claims for refund for the years 1936, 1937 and 1938 (R. 17). These claims were based on the ground that the credit for foreign taxes should have been computed according to the following formula (R. 15):

$$\text{Foreign Tax accrued or paid} \times \frac{\text{Dividends received}}{\text{Accumulated profits of subsidiary}} = \text{Credit allowable under § 131(f)}$$

It thus appears that the difference between the petitioner's formula for the computation of the credit and that used by the Commisioner, is that the Commissioner's

formula reduces the credit by the ratio of the "accumulated profits" to the "total profits" in the case of each subsidiary.

The claims for refund referred to were rejected on May 21, 1940. Each claim was rejected on the sole ground that the decision of the Court of Claims in *International Milling Company* v. *United States*, 89 C. Cls. 128, 27 F. Supp. 592 (1939), "has not been acquiesced in by the Commissioner" (R. 18). On February 6, 1941, the petitioner filed three new claims for the years 1936, 1937 and 1938 upon the same grounds. These new claims were filed because of the possibility that the first claims might be regarded as defective since they were filed before a portion of the tax was paid. The new claims were rejected on April 22, 1941 (R. 18). Suits were filed in the Court of Claims following the rejection of each set of claims for refund. These suits were consolidated for hearing and resulted in a single judgment. The Court of Claims held that its prior decision in *International Milling Company* v. *United States*, 89 C. Cls. 128 (1939), was not controlling and entered judgment for the United States.

Specification of Errors to be Urged.

The Court of Claims erred:

1. In holding that under a proper construction of § 131(f) of the Revenue Acts of 1936 and 1938 the credit for foreign taxes paid should be reduced by the ratio of "accumulated profits" to the "total profits" of the taxpayer's subsidiaries.

2. In failing to follow its prior decision in *International Milling Company* v. *United States*, 89 C. Cls. 128 (1939).

3. In giving effect to the change of interpretation made by the Treasury Department and first embodied in Art. 698

of Regulations 77, promulgated in 1933, twelve years after the statute was first passed, and contrary to the construction given to the statute by the Treasury contemporaneously with its enactment and consistently for many years thereafter.

4. In entering judgment for the United States.

Reasons for Granting the Writ.

1. The decision below is in conflict with the decision of the Circuit Court of Appeals for the Third Circuit in *Aluminum Company of America* v. *United States*, 123 F. (2d) 615, decided October 31, 1941. It is also in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *F. W. Woolworth and Co.* v. *United States*, 91 F. (2d) 973. This conflict is recognized in the opinion of the Court below, where the Court says (R. 24):

> "We are aware that the United States Circuit Court of Appeals for the Second Circuit in the case of *F. W. Woolworth and Co.* v. *United States*, 91 F. (2d) 973, and the United States District Court for the Western District of Pennsylvania in the case of *Aluminum Company of America* v. *United States*, 36 F. Supp. 23, reached the conclusion which the plaintiff here urges."

The District Court decision in the *Aluminum Company* case referred to in this passage was affirmed by the Circuit Court of Appeals as indicated above.

The decision below is also inconsistent in reasoning with the decision of the Court of Claims itself just two years previous in *International Milling Company* v. *United States*, 89 C. Cls. 128, 27 F. Supp. 592. In this connection, reference is made to the succinct statement of the dissenting opinion of the Chief Justice in the court below (R. 24-25).

2. Insofar as the decision below is rested upon a change in the administrative construction of the statute made by the Treasury Department in 1931, it is in conflict with the decision of the Circuit Court of Appeals for the Third Circuit in *Commissioner* v. *Warren Webster Trust*, 122 F. (2d) 915.[1] That case involved a statutory provision which was first enacted in 1924 and which has remained unchanged since that time. Ten years later, in 1934, the Treasury issued a regulation construing this section. The court held that this regulation was not valid saying (122 F. (2d) at 191-192):

> "The statutory provisions with which we are concerned have been contained in each Revenue Act commencing with the Revenue Act of 1924, whereas the regulations upon which the Commissioner relies were first adopted in 1934, ten years later. During that period of ten years, the Commissioner did not suggest the interpretation for which he now contends. His belated change in view can hardly be imputed to Congress."

In the present case, the situation is even stronger. Here the statute was first enacted in 1921. It is clear that the contemporaneous construction of the Treasury was in accordance with the petitioner's contention, and this construction was followed by the Treasury for ten years. In 1933, the Commissioner changed his regulations so as to state the rule for which he now contends (see Appendix, *infra*, pp. 11-12). The words of the Third Circuit seem directly applicable: "His belated change in view can hardly be imputed to Congress."

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[1] See also *Commissioner* v. *Title Guaranty and Trust Co.*, decided by the Second Circuit Court of Appeals on December 1, 1941, on the sole authority of the Third Circuit decision in *Commissioner* v. *Warren Webster Trust*.

To the same effect are this Court's decisions in *Helvering* v. *Janney*, 311 U. S. 189; *Taft* v. *Helvering*, 311 U. S. 195, and *Helvering* v. *Oregon Mutual Life Ins. Co.*, 311 U. S. 267.[2]

3. The decision below is erroneous. Although Congress expressly amended the statute in 1921, and changed its language from what it had been in § 240(c) of the Revenue Act of 1918, the decision construes the 1921 Act to have the same meaning as the 1918 law, thus denying any effect to the change which Congress made. In reaching this result, the decision ignores the specific statement of Senator Smoot, in charge of the Bill on the floor of the Senate, when in explaining the amendment of the Senate which became § 238(e) of the Revenue Act of 1921 (which has remained in effect without change to this day), he dealt with the specific situation now before the court and stated plainly the conclusion for which the petitioner now contends and which was contemporaneously accepted by the Treasury Department. Senator Smoot's statement is as follows (61 Congressional Record, Part 7, p. 7184, November 2, 1921):

> "Assume that the foreign corporation accumulated a surplus of $200,000.00 upon which it has paid income and profits taxes of $80,000.00, leaving $120,000.00 of disposable or distributable surplus. Assume further that it actually pays dividends to the American parent company of $50,000.00, i.e., of five-twelfths of its disposable surplus. Then the American parent company may take credit for five-twelfths of the $80,000.00 taxes

[2] *Helvering* v. *Janney* (p. 195): "This we think was the meaning of the provision of the Revenue Act of 1934 when it was enacted, and it was subject to change only by Congress, and not by the Department."

Taft v. *Helvering* (p. 198): "We are of the opinion that under the Revenue Act of 1934, taken with the meaning we think it had when enacted, petitioners were entitled to the combined deductions they claimed, and that the departmental regulation to the contrary was ineffective to deprive them of that right."

Helvering v. *Oregon Mutual Life Ins. Co.* (p. 272): "For it is our conclusion that by § 203(a)(2) of the 1932 and 1934 Acts, Congress has granted life insurance companies a deduction for disability reserves which only Congress can take away."

> which the foreign subsidiary paid, i.e., it may take credit for $33,333.33."

After Senator Smoot's explanation, Senator Simmons, the ranking minority member, said (61 Congressional Record, Part 7, p. 7184):

> "With that statement of the purpose and effect of the amendment, I shall have no objection to it. I think it is entirely fair."

Though the specific statement by Senator Smoot, in charge of the bill, is directly in accordance with the petitioner's contention, the court below dismissed it as "inadvertent" (R. 23).

In this connection, the attention of the court is invited to the opinion of Judge Green writing for the Court of Claims in *International Milling Company* v. *United States*, 89 C. Cls. 128, 27 Fed. Supp. 592 (1939). Not only is the argument there persuasive, but it seems not irrelevant to point out that Judge Green had exceptional qualifications to speak of the attitude of Congress in such a matter. Judge Green was for many years the Chairman of the Ways and Means Committee of the House of Representatives. He was a member of that Committee at the time of the enactment of the Revenue Act of 1921. He was a member, for the House, of the Conference Committee in 1921 which accepted the amendment made on the floor of the Senate by which the language in question was introduced into the Bill. Judge Green's view was that the formula used by the Commissioner and now upheld by the court below, is "merely a mathematical device for avoiding the method prescribed by the statute." 89 C. Cls. at 136, 27 Fed. Supp. at 596.

4. The decision below involves a question of importance in the administration of the revenue laws. The question raised is one which must be determined in connection with the return of any taxpayer which has a foreign subsidiary

and is entitled to the credit provided by § 131(f). The resolution of the uncertainty engendered by the decision below is a matter of importance in the efficient administration of the revenue laws.

WHEREFORE; it is respectfully submitted that this petition for a writ of certiorari should be granted.

ERWIN N. GRISWOLD,
Counsel for Petitioner.

January, 1942.

APPENDIX.

Statutes and Regulations Involved.

STATUTES.

Section 131 of the Revenue Act of 1936 provides as follows:

"(a) Allowance of Credit.—If the taxpayer signifies in his return his desire to have the benefits of this section, the tax imposed by this title shall be credited with:

"(1) Citizen and Domestic Corporation.—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States;

* * * * * * *

"(f) Taxes of Foreign Subsidiary.—For the purposes of this section a domestic corporation which owns a majority of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall be deemed to have paid the same proportion of any income, war-profits, or excess-profits taxes paid by such foreign corporation to any foreign country or to any possession of the United States, upon or with respect to the accumulated profits of such foreign corporation from which such dividends were paid, which the amount of such dividends bears to the amount of such accumulated profits: Provided, That the amount of tax deemed to have been paid under this subsection shall in no case exceed the same proportion of the tax against which credit is taken which the amount of such dividends bears to the amount of the entire net income of the domestic corporation in which such dividends are included. The term 'accumulated profits' when used in this subsection in reference to a foreign corporation, means the amount of its gains, profits, or income in excess of the income, war-profits, and excess-profits or income;

and the Commissioner with the approval of the Secretary shall have full power to determine from the accumulated profits of what year or years such dividends were paid; treating dividends paid in the first sixty days of any year as having been paid from the accumulated profits of the preceding year or years (unless to his satisfaction shown otherwise), and in other respects treating dividends as having been paid from the most recently accumulated gains, profits, or earnings. In the case of a foreign corporation, the income, war-profits, and excess-profits taxes of which are determined on the basis of an accounting period of less than one year, the word 'year' as used in this subsection shall be construed to mean such accounting period."

Section 131(f) of the Revenue Act of 1938 is the same, and this is continued to the present time in § 131(f) of the Internal Revenue Code. These provisions are not different in any material respect from the corresponding provision in every Revenue Act beginning with that of 1921.

Regulations.

The first Regulations issued after the enactment of the Revenue Act of 1921 was Regulations 62, promulgated February 15, 1922. Articles 383 and 612 of Regulations 62 provide that a domestic corporation owning the majority of the stock of a foreign corporation should seek its credit for foreign taxes by filing Form 1118 "with the calculations of credit there indicated." Form 1118 thus indicated and incorporated into the Regulations provided for the calculation of the credit in accordance with the Petitioner's contentions.

The Regulations issued under the ensuing Revenue Acts through the Revenue Act of 1928 were the same. Each made reference to Form 1118, and Form 1118 continued to provide for the calculation of the credit in accordance with the petitioner's contentions. The references are as follows:

Rev. Act of 1924, Regulations 65, Articles 386, 612;
Rev. Act of 1926, Regulations 69, Articles 383, 612;
Rev. Act of 1928, Regulations 74, Articles 693, 698.

The first Regulation establishing a contrary rule was Regulations 77, under the Revenue Act of 1932, and promulgated February 10, 1933. Article 698 of Regulations 77 provides for the computation of the credit in accordance with the contentions of the Government. This Article has been unchanged so far as the present question is concerned in the Regulations issued under subsequent Revenue Acts. It is now found as § 19.131-8 of Regulations 103.